

A&P

The Great Atlantic & Pacific Tea Company, Inc.



1996 Annual Report

delivering
the
difference
meeting
diverse
needs

A&P

The Food Emporium

PHARMACY DEPT.

A&P
FOOD MARKET

**food
Basics**
Bottom Line Prices!!!

FARMER
JACK

Dominion

waldbaums

**SUPER
fresh**
FOOD MARKET

kohl's

Comparative Highlights

	<i>The Great Atlantic & Pacific Tea Company, Inc.</i>		
<i>(Dollars in thousands, except per share amounts)</i>	Fiscal 1996	Fiscal 1995	Fiscal 1994
Sales	\$10,089,014	\$10,101,356	\$10,331,950
Income (loss) from operations	169,303	151,734	(57,530)
Income (loss) before cumulative effect of accounting change	73,032	57,224	(166,586)
Net income (loss)	73,032	57,224	(171,536)
Income (loss) per share before cumulative effect of accounting change	1.91	1.50	(4.36)
Net income (loss) per share	1.91	1.50	(4.49)
Cash dividends per share	.20	.20	.65
Expenditures for property	296,878	236,139	214,886
Depreciation and amortization	230,748	225,449	235,444
Working capital	215,374	190,967	97,277
Shareholders' equity	890,072	822,785	774,914
Debt to total capitalization	.49	.49	.53
Book value per share	23.27	21.53	20.27
New store openings	30	30	22
Number of stores at year end	973	1,014	1,108
Number of franchised stores served at year end	49	7	—

Company Profile

The Great Atlantic & Pacific Tea Company, Inc. ("the Company"), based in Montvale, New Jersey, operates conventional supermarkets and larger superstores in 19 U.S. states, the District of Columbia and Ontario, Canada, under the A&P, Waldbaum's, Food Emporium, Super Fresh, Farmer Jack, Kohl's, Sav-A-Center, Dominion, and Food Basics trade names. As of the fiscal year ended February 22, 1997, the Company operated a total of 973 stores, and served 49 franchised stores. Through its Compass Foods Division, the Company also manufactures and distributes a line of coffees under the Eight O'Clock, Bokar and Royale labels, both for sale through its own stores and by other companies outside of A&P's trading areas.

About the Cover

This year's annual report focuses on "Delivering the Difference By Meeting Diverse Needs." Our stores, products, and employees, are all committed to providing for the diverse shopping requirements of our customers. By providing a wide range of services we continue to expand with the expectations of the weekly shopping trip. From enhanced grocery offerings, expanded produce and prepared foods departments, frequent shopper cards, pharmacies, and banking services in bigger, better stores, we're delivering the difference.

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Letter to Shareholders



A&P made solid progress in 1996, as we continued the turn-around in Canada and the revitalization of our store base in key U.S. markets.

For the year ended February 22, 1997, A&P achieved a 28% increase in net income, from \$57.2 million to \$73.0 million, and from \$1.50 to \$1.91 per share. Sales were \$10.1 billion, about the same as the previous year, as we continued to close older, outmoded stores and replace them with new, modern state-of-the-art superstores.

Total sales turned up in the second half of the year and total square footage, including franchise stores, increased 2.1%. Net income was the highest since 1990 and our selling, general and administrative expense rate the lowest since 1991. We accelerated the turnaround in Canada and moved forward with new store development, merchandising initiatives and profit improvement measures. In Michigan, Farmer Jack results continued to progress in earnings, sales and market share achievements.

A&P's business goal is to grow our earnings and reward our investors with better than industry average returns. Our strategy for achieving that goal is to build dominant market share in our major marketing areas. We did this throughout the 1980's and our store base continues to evolve in the 1990's.

A&P is driven by the market – which is really the varied needs of the customers we serve. Each of our regional chains operate stores that are designed and merchandised to appeal to customer profiles in their individual markets. Chainwide, however, we are following a basic 4-point strategy in meeting these diverse needs by:

- *Replacing smaller stores with large superstores that provide exceptional customer appeal.*
These new stores – often providing 50,000+ square feet in shopping space – are reshaping A&P's image in the marketplace and helping attract many new shoppers.
- *Featuring the finest perishable departments.*
For example, a prime goal is to become the leading produce merchant wherever we operate. The expansive farmer's market concept we have introduced in our stores is a key to making this concept work. Other departments where we emphasize quality and service include fresh meat, seafood, bakery, take-out foods, deli and pharmacies.
- *Creating unique customer appeal through industry-leading private labels.*
One way in which we differentiate our stores is by offering the customer store brands which provide equal or better quality at prices below those of comparable national brands. Names such as *Master Choice*, *America's Choice* and *Eight O'Clock Coffee* help us build a franchise with shoppers.
- *Emphasizing product category management by tailoring each store's offerings to its local market.*
Product category management enables us to put the right quantities of the right items in each market to service the needs of our customers, while still meeting our sales and profit objectives. Its goal is to reduce out-of-stock items and generate higher sales with less inventory.



(left to right)

James Wood
*Chairman of the Board and
 Co-Chief Executive Officer*

Christian W.E. Haub
*President and
 Co-Chief Executive Officer*

We are using this strategy in our key markets to build on our strengths and solidify long-term profitability. Metro New York, Ontario, Canada and Michigan are major markets where we have strong market shares that serve as the basis for our future growth.

Ontario, Canada

Our progress in Canada was key to our success last year. We converted 41 loss-making conventional stores in Ontario to the successful Food Basics format, which is targeted to the price sensitive segment of its market. We expect to open or convert another 20+ Food Basics stores in 1997. Dominion stores, which are geared to the quality/service market segment in Toronto, also showed positive sales and profit trends during the year. These two store groups, together with our A&P/Super Fresh stores outside the Metro Toronto area, give us a potent combination of store formats in Ontario.

Metro New York

In the United States, our metropolitan New York operations moved forward despite a difficult sales environment. Waldbaum's, which is being re-established as Long Island's strong market leader, showed improving sales trends throughout the year. In 1997, Waldbaum's will begin adding new stores for the first time in several years with six projects under development. The A&P group in the Metro area continued to open new superstores and close older, outmoded facilities delivering a more rewarding shopping experience to a growing number of customers. Metro A&P opened nine new or replacement stores in 1996 and has ten more scheduled for this year. The upscale Food Emporium chain again turned in an outstanding financial performance and continues to expand. Our first Food Emporium in New Jersey recently opened on April 26th in Fort Lee, replacing a smaller A&P store.

Midwest

In the midwest, Farmer Jack is the clear market leader in the Metro Detroit Michigan market area and has gained three percentage points in market share over the past two years. The seven new stores planned in 1997 will help continue this strong growth trend. The Kohl's stores in Wisconsin have been able to maintain consistently good results in a market dominated by discount stores. Kohl's will add three new stores this year as we expand our commitment to the quality store segment there.

Mid-Atlantic

Super Fresh operates in the Mid-Atlantic states with 69 stores in Philadelphia's Delaware Valley and 68 in the Baltimore/Washington D.C. area. These two groups are well-positioned for future growth in their markets. We added ten new stores last year and ten more are scheduled in 1997.

In those groups where we have lower market shares, we are selectively investing in new stores in order to maintain our competitive positions. In New England, we opened two new stores very successfully in 1996 and have three more scheduled this year. The New England market has seen some dramatic changes in competitive ownership during the past year, which has given our A&P and Waldbaum's Food Mart stores some unique opportunities.

In the South and Southeast we opened one new store each in Atlanta and New Orleans in 1996, and have two planned for Atlanta in 1997. In the Carolinas and Virginia, our South Central Group will continue to optimize results through its Farmer Jack and Super Fresh stores by emphasizing the best perishables in the marketplace, particularly produce. Our plan is to maintain these historic A&P markets which are small country stores, in the main, as a basis for possible future development.

Our new '90s generation of superstores are state-of-the-art and at least equivalent to the best in each of our many marketplaces. The development of these superstores is confined to our core markets and their success throughout the '90s has been excellent from a sales and profit point-of-view.

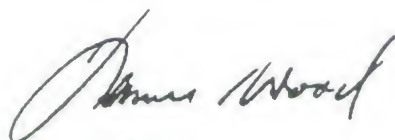
The new A&P superstores have accelerated the obsolescence of some existing stores, particularly in our core markets, which in the short term has created adverse sales and profits in the older stores. By the end of 1998, with 92% of A&P sales expected to come from stores that have been either opened or remodeled in the '90s, this short-term problem will be at an end.

In 1997, we plan to open 40 superstores. To implement this plan and make the needed upgrades and modernization of other facilities, we have allocated \$310 million for capital spending in 1997, up from \$297 million in 1996.

The supermarket industry today is adjusting to a continually changing society. Lifestyles have changed, people have less time to shop and prepare meals. Food at home as a percentage of disposable income has been reduced from 9.1% in 1980 to 6.5% in 1996, exacerbated by the growing number of warehouse clubs, super drug stores and other channels of distribution that continue to expand their food variety offering. Food away from home, until recently the supermarket's major competitor, has remained at 4.2% of disposable income for a number of years.

A&P has been in the food business for 138 years. The Company has survived through tremendous changes in that period and has made important moves to adjust to customers' needs. This fiscal year will be the year of transition from my tenure as Chief Executive Officer to that of the next, Christian Haub, a son of the major stockholder, who was recently appointed Co-Chief Executive Officer. He and other members of management look forward to meeting the challenges of the next century with great experience and confidence. Our Board of Directors indicated their confidence on March 18, 1997 when they voted an increase in the regular quarterly dividend from 5 cents to 10 cents per share.

Having come through a difficult period in the early '90s we are well prepared to resume the industry leadership and growth of sales and profits we had in the '80s. With an improving store base, dominant market shares in our core business, a sound balance sheet, and a well-trained management succession team to take over the helm in the future, we believe that 1997 and the years following will be rewarding for our employees, our customers, the communities we serve and our shareholders.



James Wood
*Chairman of the Board and
Co-Chief Executive Officer*

Canada's leader for quality & selection



Our successful Farmers' Market look has now been extended through all of our Dominion produce departments, as illustrated above.

Throughout the store — from the exterior window signs, the aisle displays to banners throughout the store — our competitive low prices and special values are communicated.



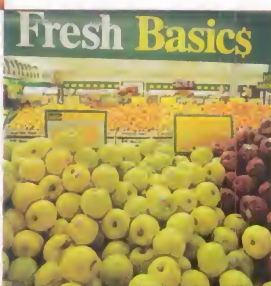
Value throughout the store, everyday



In Canada, our Dominion, Food Basics and A&P/Super Fresh stores are proving every day that filling customers' varied needs adds up to a winning formula. In the Toronto metro area, 55 Dominion supermarkets offer an array of upscale items that keep discriminating urban and suburban shoppers coming back for more.

Delivering the Difference

By Meeting Diverse Needs...



Ontario is also home to 56 Food Basics stores, of which 49 are franchised. These stores provide a competitively-priced, limited selection that's right on target for its cost-conscious clientele. Outside the Toronto area, 114 stores bearing the A&P/Super Fresh banners are pleasing their upper-middle market customers with great produce and other perishable departments.

A dramatic turnaround in Canada was A&P's biggest success story last year. With continuing store conversions to Food Basics in the works, the prospects for 1997 are even brighter.

New stores fulfilling every desire



Today's customers are looking for quality *and* convenience. Our stores, including the new Kenilworth store pictured above, feature carry out selections geared towards meeting the demands of busy consumers.

Food Emporium — located in Manhattan at 68th Street and Third Avenue, shown below, is one of several two floor supermarkets where shoppers travel from the bakery and deli

— conveniently located on the ground floor for their daily shopping trip — to the full service supermarket below, perfect for their weekly shopping trip.



Great locations & spectacular service



metropolitan New York area shoppers have good reasons to call the local A&P or Food Emporium “their store.”

From Manhattan to New Jersey to Westchester County where do busy New Yorkers go for an upbeat, convenient shopping experience? To one of A&P's many New York area Superstores, where they find an expansive store with pleasant surroundings, wide aisles and a vast assortment of quality items. In a single outing, the Superstore customer can satisfy a host of shopping needs at outstanding departments such as produce, bakery, butcher shop, seafood, take-out and deli — and partake of such added services as a pharmacy, drug store, florist, and a bank branch. Everything to satisfy your weekly shopping needs.



Delivering the Difference

Our new A&P stores fulfill all the needs of the weekly shopping trip including the conveniences of in-store full branch banking.



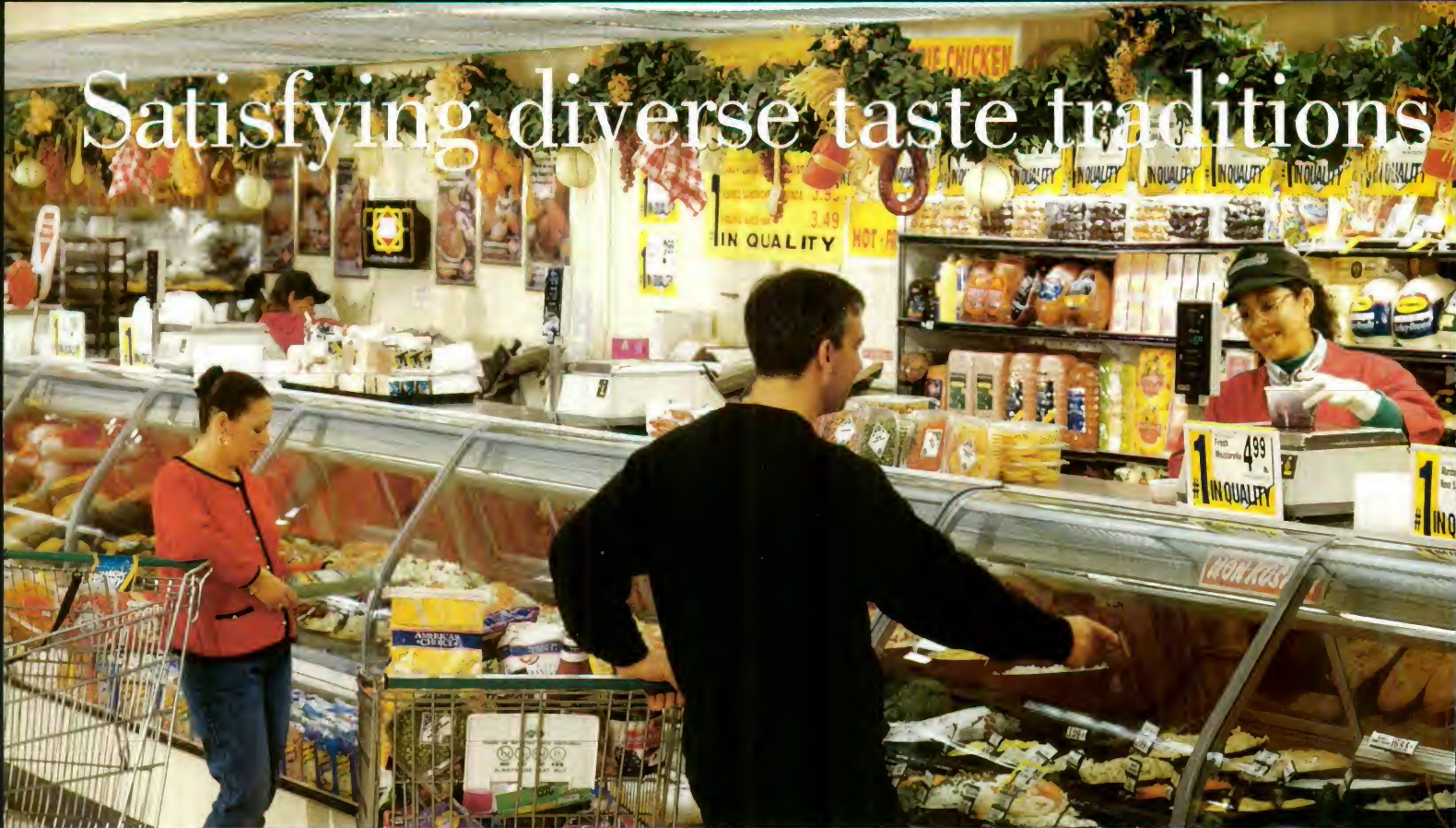
By Meeting Diverse Needs...

The Food Emporium



In a different approach, the New York area's 34 Food Emporiums are establishing a gourmet tradition with distinctive, top-of-the-line domestic and imported food products and carriage trade-style customer service. While most Food Emporiums are in Manhattan, larger stores serve leading neighborhoods in Westchester, Long Island, Connecticut and, most recently, Northern New Jersey.

Satisfying diverse taste traditions



The Waldbaum's delicatessen is the place our customers fulfill their traditional food desires. From seasonal specialties, to everyday favorites, we deliver quality and value.

Below, our Fairless Hills, Pennsylvania store grand opening was one of ten new Super Fresh stores opened in 1996 — with ten more planned for 1997.



Convenient new locations for customers



Meanwhile, competitive pricing and ethnic appeal characterize Waldbaum's 89 stores in New York City, Long Island and Westchester County, New York. Waldbaum's serves the needs of shoppers searching for traditional foods and services, many of them with Jewish, Italian or Hispanic roots. At Waldbaum's, they know they'll find the food items that satisfy their special tastes at value-oriented prices.

Delivering the Difference



By Meeting Diverse Needs...



If the Waldbaum's chain in Metro New York specializes in traditional neighborhood appeal, then Super Fresh is A&P's Mid-Atlantic proving ground for new ideas.

Super Fresh, with 179 stores in the Philadelphia, Baltimore, Washington, D.C. and Virginia markets, is a supermarket chain of firsts. It was the first in the A&P system to install automated scanners in check-out counters, one of the first to feature expanded produce departments, and the first to introduce A&P's Bonus Savings Club frequent shopper program now in use system-wide. Shoppers use their Bonus Savings card both to obtain discounts on qualifying items and as a check-cashing card.



It's always savings time at Farmer Jack



New Farmer Jack stores have been opening at a rapid rate over the last several years — making it the fastest growing chain in the Midwest.

Many of the attributes of the Food Emporium have found a home in Wisconsin under the Kohl's banner.

Kohl's continues to build its franchise in the quality and service market segment.



Kohl's: the Wisconsin tradition of Quality



When their customers speak, Farmer Jack and Kohl's listen — which, no doubt, helps explain the success of this pair of thriving supermarket chains in America's heartland.

Farmer Jack operates 99 stores in Michigan and pioneered the value-oriented, high volume approach to super-marketing in the Midwest. Most Farmer Jack stores feature 24-hour service and one-stop shopping convenience including drug store/pharmacy, extensive take-out foods and expanded perishable and service departments. The group prides itself on the close relationships Farmer Jack people have in store communities.

Delivering the Difference

Farmer Jack's Grab 'N Go carry out section, pictured above, meets the needs of the fast-paced, 24-hour lives of Detroit's residents.

By Meeting Diverse Needs...

kohl's



Kohl's is just as deeply rooted in the traditions of its home state, Wisconsin. At its 47 stores, Kohl's offers quality perishable departments like produce, bakery and deli, and a wide selection of items in all categories. Kohl's has been one of A&P's most consistent revenue and profit producers over the years.

Building on its Midwestern success last year, A&P plans to open seven new Farmer Jack and three new Kohl's stores in 1997.

Delivering valued product selections



Real Value. Real Savings.
The concept of America's
Choice — over 1,500
private label products sold

throughout our stores —
are brought to customers by
these traveling billboards.

With over 400 premium
private label products,
the Master Choice line
has become synonymous
with quality.



Exceptional quality and taste



a&P clearly had a range of customer preferences in mind when it created its “America’s Choice” and “Master Choice” private labels.

“America’s Choice,” introduced in 1993 throughout the A&P system, is designed for shoppers who want quality at an attractive price. *The New York Times* confirmed in a 1996 feature article that “America’s Choice” items were comparable to national brands in quality, but priced substantially lower.

Delivering the Difference

By Meeting Diverse Needs...



for customers with more selective tastes, A&P created “Master Choice.” This label competes with gourmet and other premium foods, but still sells for less than comparable national brands. A third A&P private label, one that meets shoppers’ health and beauty care needs, is “Health Pride.”



What’s the most successful private label in all of food retailing? It’s “Eight O’Clock Coffee,” which dates back to A&P’s beginnings. “Eight O’Clock’s” appeal is almost universal: It’s for everyone who likes a great tasting cup of coffee!

OPERATING RESULTS

Fiscal 1996 Compared with 1995

Sales for fiscal 1996 were \$10,089 million, a net decrease of \$12 million or 0.1% when compared to fiscal 1995 sales of \$10,101 million. U.S. sales decreased \$83 million or 1.0% compared to fiscal 1995. U.S. same store sales, which include replacement stores, were down 0.7% from the prior year. In Canada, sales increased \$71 million or 4.1% from fiscal 1995 to \$1,807 million. Canada same store sales, which include replacement stores, were up 0.5% from the prior year.

Total Company same store sales, including replacement stores, for fiscal 1996 decreased 0.5% from the prior year. Average weekly sales per supermarket were approximately \$195,200 in fiscal 1996 versus \$183,300 in fiscal 1995 for a 6.5% increase. During fiscal 1996, the Company opened 27 new supermarkets and 3 new liquor stores, remodeled or expanded 72 stores, and closed 71 stores, of which 23 were converted to Food Basics franchised stores in Canada.

The sales decrease of \$12 million from last year was mainly the result of store closings. The Company closed 171 stores, excluding replacement stores, since the beginning of fiscal 1995 which reduced comparative sales by approximately \$443 million or 4.4% in fiscal 1996. The store closures include 41 stores that were subsequently converted to Food Basics franchised stores. The lost sales of the store closures were offset by the opening of 35 new stores, excluding 25 stores that replaced 27 older, outmoded stores, since the beginning of fiscal 1995 which increased sales by approximately \$276 million or 2.7% in fiscal 1996. In addition, the opening and conversion of 42 Food Basics franchised stores in fiscal 1996 increased wholesale sales to the Franchisees by \$199 million to sales of \$205 million in fiscal 1996, from sales of only \$6 million in fiscal 1995.

Gross margin as a percent of sales decreased 0.1% to 29.0% for the current year from 29.1% for the prior year resulting primarily from lower margins on wholesale sales to the Food Basics franchised stores, partially offset by an increase in the retail supermarket margin in both the U.S. and Canada. The gross margin dollar decrease of \$14 million is primarily the result of a decrease in gross margin rates of \$10 million, a decrease in sales volume which had an impact of decreasing margin by \$6 million, partially offset by a higher Canadian exchange rate resulting in an increase of \$2 million. The U.S. gross margin increased \$16 million principally as a result of increased gross margin rates of \$40 million, partially offset by a decrease in sales volume which had an impact of decreasing margin by \$24 million. In Canada, gross margin decreased \$30 million, primarily resulting from the effect of a decrease in gross margin rates of \$50 million, partially

offset by sales volume increases which impacted margins by \$18 million, and a higher Canadian exchange rate resulting in an increase of \$2 million.

Store operating, general and administrative expense of \$2.752 million in fiscal 1996 declined by approximately \$31 million from fiscal 1995. As a percent of sales, store operating, general and administrative expense for fiscal 1996 decreased to 27.3% from 27.6% for the prior year. U.S. expenses increased \$19 million, principally as a result of increased store labor and rental costs on the new superstores opened in fiscal 1996. Canadian expenses decreased \$50 million, principally as a result of reduced store labor and occupancy costs as a result of converting 41 stores to Food Basics franchised stores.

Interest expense increased \$0.1 million from the previous year, primarily due to increased average borrowings in the U.S. partially offset by lower average interest rates.

Interest income increased \$2.0 million from the previous year, primarily due to interest income on equipment leases and inventory notes relating to the Food Basics franchise business.

Income before taxes for fiscal 1996 was \$101 million as compared to \$81 million in fiscal 1995 for an increase of \$20 million or 24%. Income before taxes increased due to improvements in the results of the Canadian operations of \$24 million from \$8 million in fiscal 1995 to \$32 million in fiscal 1996. The Canadian increase was partially offset by a decrease in U.S. income before taxes from \$73 million in fiscal 1995 to \$69 million in fiscal 1996.

The effective tax rate for fiscal 1996 was 27.4% as compared to a tax rate of 29.4% in fiscal 1995. Included in the fiscal 1995 tax provision is a \$6.5 million or \$0.17 per share credit relating to a refund of previously paid taxes in Canada. Excluding the \$6.5 million credit, the fiscal 1995 income tax provision would have been \$30.4 million resulting in an effective tax rate of 37.4%. The decrease in the effective tax rate, after giving effect to this credit is mainly attributable to the change in the Canadian income tax valuation allowance. The Company is reversing the income tax valuation allowance to the extent that its Canadian operations generate taxable income.

During fiscal 1994, the Company recorded a valuation allowance of \$119.6 million against Canadian deferred tax assets, which, based upon current available evidence, are not likely to be realized. These deferred tax assets resulted from tax loss carryforwards and deductible temporary differences arising from the Canadian write-off of goodwill and long-lived assets.

During fiscal 1996, since the Canadian operations generated pretax earnings, the Company reversed approximately \$14.3 million of the valuation allowance. Although Canada generated

pretax earnings in fiscal 1996 of \$32 million and \$8 million in fiscal 1995, the Company was unable to conclude that the Canadian deferred tax assets were more likely than not to be realized. This conclusion was based in part on the competitive Canadian marketplace and the significant losses experienced prior to fiscal 1995. Accordingly, at February 22, 1997 the Company is continuing to fully reserve its Canadian net deferred tax assets. The valuation allowance will be adjusted when and if, in the opinion of Management, significant positive evidence exists which indicates that it is more likely than not that the Company will be able to realize the Canadian deferred tax assets.

Net income for fiscal 1996 was \$73 million or \$1.91 per share as compared to \$57 million or \$1.50 per share for fiscal 1995. Excluding the \$6.5 million or \$0.17 per share Canadian tax refund, fiscal 1995 net income would have been \$51 million or \$1.33 per share. Accordingly, excluding the effect of such refund, net income increased \$22 million or \$0.58 per share. The increase in net income is the result of lower store operating, general and administrative expenses of \$31 million, coupled with a lower effective income tax rate, partially offset by lower gross margins of \$14 million.

Fiscal 1995 Compared with 1994

Sales for fiscal 1995 were \$10,101 million, a net decrease of \$231 million or 2.2% when compared to fiscal 1994 sales of \$10,332 million. U.S. sales decreased \$176 million or 2.1% compared to fiscal 1994. U.S. same store sales, which include replacement stores, were down 0.2% from the prior year. In Canada, sales of \$1,736 million decreased \$55 million or 3.1% from fiscal 1994. Canada same store sales, which include replacement stores, were down 1.6% from the prior year.

During fiscal 1995, the Company opened 27 new supermarkets and 3 new liquor stores, remodeled or expanded 76 stores, and closed 124 stores, of which 6 were converted to Food Basics franchised stores in Canada, and 8 in the Rhode Island market which were sold to Edwards Super Food Stores in the first quarter of fiscal 1995. The Company recorded sales to the Food Basics franchised stores of \$6 million in fiscal 1995. The Company closed 190 stores, excluding replacement stores, since the beginning of fiscal 1994. The store closures, excluding replacement stores, since the beginning of fiscal 1994 reduced comparative sales by approximately \$422 million or 4.1% in fiscal 1995. The opening of 33 new stores, excluding 19 stores that replaced 21 older, outmoded stores, since the beginning of fiscal 1994 added approximately \$219 million or 2.1% to sales in fiscal 1995.

Total company same store sales, including replacement stores, for fiscal 1995 decreased 0.5% from the prior year. Average weekly sales per supermarket were approximately \$183,300 in fiscal 1995 versus \$176,000 in fiscal 1994 for a 4.1% increase.

Gross margin as a percent of sales increased 0.6% to 29.1% for the current year from 28.5% for the prior year resulting primarily from increased gross margin rates in both the U.S. and Canada partially offset by increased promotional price reductions in the U.S. The gross margin dollar decrease of \$8 million is primarily the result of a decrease in sales volume which had an impact of decreasing margin by approximately \$69 million, partially offset by an increase in gross margin rates of \$58 million and an increase in the Canadian exchange rate of \$3 million. The U.S. gross margin decreased \$17 million principally as a result of decreased sales volume which resulted in margins decreasing \$50 million partially offset by an increase in gross margin rates of \$33 million. In Canada, gross margin increased \$9 million, primarily resulting from the effect of an increase in gross margin rates of \$25 million and a higher Canadian exchange rate resulting in an increase of \$3 million, partially offset by sales volume declines which impacted margins by \$19 million.

Store operating, general and administrative expense of \$2,784 million in fiscal 1995 declined by approximately \$90 million from fiscal 1994. The fiscal 1994 store operating, general and administrative expense includes charges of \$27 million for employee buy-out costs incurred as a result of new labor agreements entered into in Canada and \$17 million to cover the cost of closing 13 stores, other than Miracle Food Mart ("Miracle") stores in Canada. As a percent of sales, store operating, general and administrative expense for fiscal 1995 decreased to 27.6% from 27.8% for the prior year. U.S. expenses decreased \$4 million, principally as a result of lower store labor costs on reduced sales volume. Canadian expenses decreased \$86 million, as a result of the charges noted above of \$27 million and \$17 million recorded in fiscal 1994, coupled with reduced store labor costs and reduced occupancy costs.

Included under the Company's 1995 year-end balance sheet captions "Other accruals" and "Other non-current liabilities" are amounts totaling approximately \$23 million associated with store closing liabilities. During fiscal 1995 approximately \$20 million was charged against the store closing reserve.

During fiscal 1994, the Company recorded a charge of \$127 million representing the write-off of \$50 million of goodwill and the write-down of \$77 million of fixed assets relating to Miracle stores which were expected to continue to generate operating losses.

As of February 24, 1996, based on current information, the Company has no reasonable basis to believe that there has been any further impairment of its existing goodwill. There is currently no goodwill recorded relating to the Canadian operations.

Interest expense increased \$0.2 million from the previous year, primarily due to increased Canadian borrowings and an increase in average interest rates. U.S. interest expense decreased from the previous year, as a result of decreased borrowings and a decrease in average interest rates on short-term borrowings.

Income before taxes and cumulative effect of accounting change for fiscal 1995 was \$81 million as compared to a loss of \$129 million in fiscal 1994. The fiscal 1994 loss included Canadian charges for the write-off of goodwill and long-lived assets of \$127 million, the employee termination/reassignment program of \$27 million and the provision for store closings of \$17 million.

Income before taxes and cumulative effect of accounting change for U.S. operations for fiscal 1995 was \$73 million as compared to \$81 million for fiscal 1994, or an 8.9% decrease. For Canadian operations, income before taxes and cumulative effect of accounting change for fiscal 1995 was \$8 million as compared to a loss of \$210 million for fiscal 1994, resulting in an increase of \$218 million.

During fiscal 1994, the Company recorded a valuation allowance of \$119.6 million against Canadian deferred tax assets, which, based upon current available evidence, are not likely to be realized. These deferred tax assets result from tax loss carryforwards and deductible temporary differences arising from the Canadian write-off of goodwill and long-lived assets.

The Company historically provided U.S. deferred taxes on the undistributed earnings of the Canadian operations. During fiscal 1994, the Company made an election to permanently reinvest prior years' earnings and, accordingly, reversed deferred tax liabilities of \$27 million associated with the undistributed earnings of the Canadian operations. Further, this decision also resulted in a direct charge to equity of approximately \$20 million to eliminate the deferred tax asset related to the Cumulative Translation Adjustment.

During fiscal 1995, since the Canadian operations generated pretax earnings, the Company reversed approximately \$3.4 million of the valuation allowance. Although Canada generated pretax earnings in fiscal 1995, the Company was unable to conclude that realization of such deferred tax assets was more likely than not due to pretax losses experienced by Canada in prior years. Accordingly, at February 24, 1996 the Company is continuing to fully reserve its Canadian net deferred tax assets. The valuation allowance will be adjusted when and if, in the

opinion of Management, significant positive evidence exists which indicates that it is more likely than not that the Company will be able to realize the Canadian deferred tax assets.

In addition, during fiscal 1995 the Company recorded a \$6.5 million credit relating to a refund of previously paid taxes in Canada.

Effective February 27, 1994, the Company adopted Statement of Financial Accounting Standards No. 112, "Employers' Accounting for Postemployment Benefits" ("SFAS 112"). As a result, in fiscal 1994 the Company recorded an after-tax charge of \$5 million or \$0.13 per share as the cumulative effect of this change on prior years.

Net income for fiscal 1995 was \$57 million or \$1.50 per share as compared to a net loss for fiscal 1994 of \$172 million or \$4.49 per share. Fiscal 1995 net income included the \$6.5 million Canadian tax refund. The fiscal 1994 net loss included after-tax Canadian charges for the write-off of goodwill and long-lived assets of \$127 million, the employee termination/reassignment program of \$27 million, the provision for store closings of \$17 million, a reduction of deferred tax benefits previously recorded of \$28 million and the cumulative effect of adopting SFAS 112 of \$5 million, offset by the reversal of deferred tax liabilities of \$27 million in the U.S. associated with the undistributed earnings of the Canadian operations.

Excluding the U.S. reversal of the deferred tax liabilities associated with undistributed earnings of \$27 million recorded in fiscal 1994, net income from U.S. operations decreased from \$50 million or \$1.31 per share in fiscal 1994 to \$44 million or \$1.15 per share in fiscal 1995. Excluding the above fiscal 1994 Canadian charges and the fiscal 1995 Canadian tax refund, fiscal 1994 would have resulted in a net loss from Canadian operations of \$45 million or \$1.17 per share and fiscal 1995 would have resulted in net income of \$7 million or \$0.18 per share for a \$52 million increase.

LIQUIDITY AND CAPITAL RESOURCES

The Company ended the 1996 fiscal year with working capital of \$215 million compared to \$191 million and \$97 million at February 24, 1996 and February 25, 1995, respectively. The Company had cash and short-term investments aggregating \$99 million at the end of fiscal 1996 compared to \$100 million and \$129 million at the end of fiscal 1995 and 1994, respectively.

In December 1995, the Company executed an unsecured five year \$400 million U.S. credit agreement and a five year C\$100 million (U.S. \$73 million at February 22, 1997) Canadian credit agreement with a syndicate of banks, enabling it to borrow funds on a revolving basis sufficient to refinance any outstanding short-term borrowings. The Company pays a facility fee ranging from

3/16% to 1/2% per annum on the U.S. and Canadian revolving credit facilities. Borrowings under the U.S. revolving credit agreement were \$95 million and \$60 million at February 22, 1997 and February 24, 1996, respectively. A&P Canada has outstanding borrowings of \$59 million and \$54 million at February 22, 1997 and February 24, 1996, respectively. As of February 22, 1997, the Company has available \$305 million under its U.S. revolver and C\$19 million (U.S. \$14 million at February 22, 1997) under the Canadian credit agreement. As of February 24, 1996, the Company had available \$340 million under its U.S. revolver and C\$22 million (U.S. \$16 million at February 24, 1996) under the Canadian credit agreement. In addition, the U.S. has uncommitted lines of credit with various banks amounting to \$145 million and \$50 million as of February 22, 1997 and February 24, 1996, respectively. Borrowings under these uncommitted lines of credit amounted to \$52 million and \$35 million as of February 22, 1997 and February 24, 1996, respectively.

As of February 22, 1997, the Company has outstanding a total of \$400 million of unsecured, non-callable public debt securities in the form of \$200 million 9 1/8% Notes due January 15, 1998, and \$200 million 7.70% Notes due January 15, 2004. As of February 22, 1997, the Company has \$305 million available under the U.S. five year \$400 million revolving credit facility, accordingly, the \$200 million 9 1/8% Notes due January 15, 1998 are recorded as non-current since the Company has the ability and intent to refinance these Notes on a long-term basis. See "Indebtedness" footnote for further discussion.

On April 15, 1997, the Company issued \$300 million 7.75% 10 year Notes due April 15, 2007. The Company used the net proceeds to reduce bank borrowings under the U.S. and Canadian revolving credit facilities, prepay other indebtedness and for general corporate purposes. After reducing borrowings under the U.S. and Canadian revolving credit facilities with the net proceeds of the \$300 million Notes, the Company currently intends to draw upon the funds available under the U.S. credit facility to repay at maturity, indebtedness owing in respect of the Company's 9 1/8% Notes due January 15, 1998.

During April 1997, the Company began discussions with its lenders under its U.S. and Canadian revolving credit facilities (the "Facility") to amend such Facility to principally (i) extend the maturity; (ii) lower the cost of borrowing by reducing the spread payable over certain reference rates; and (iii) reduce the facility fees payable thereunder. Although there is no assurance that the Facility will be amended, the Company does expect to obtain such an amendment.

On October 17, 1995, the Company's Canadian subsidiary, The Great Atlantic & Pacific Company of Canada, Ltd. ("A&P

Canada"), issued U.S. \$75 million of unsecured, non-callable 7.78% Notes due November 1, 2000 guaranteed by the Company. The net proceeds from the issuance of these Notes were used to repay indebtedness under the Canadian subsidiary's revolving credit facility. In conjunction with the issuance of the U.S. \$75 million Notes, A&P Canada entered into a five year cross-currency swap agreement expiring November 1, 2000. The cross-currency swap agreement requires A&P Canada to make net payments to the counterparty based on a fixed interest differential on a semi-annual basis. The interest differential to be paid under the swap agreement is accrued over the life of the agreement as an adjustment to the yield of the 7.78% Notes and is recorded as interest expense. The Company is exposed to credit losses in the event of nonperformance by the counterparty to its currency swap. However, the Company anticipates that the counterparty will be able to fully satisfy its obligations under the contracts.

The Company's loan agreements and certain of its notes contain various financial covenants which require, among other things, minimum net worth and maximum levels of indebtedness and lease commitments. The Company was in compliance with all such financial covenants as of February 22, 1997, and believes that it will continue to be in compliance.

During fiscal 1996, the Company funded its capital expenditures, debt repayments and cash dividends through internally generated funds combined with proceeds from bank borrowings.

U.S. bank borrowings were \$147 million at February 22, 1997 as compared to \$95 million at February 24, 1996. U.S. bank borrowings during fiscal 1996 were at an average interest rate of 5.8% compared to 6.4% in fiscal 1995.

Canadian bank and commercial paper borrowings were \$59 million and \$54 million at February 22, 1997 and February 24, 1996, respectively. Canadian bank and commercial paper borrowings during fiscal 1996 were at an average interest rate of 5.3% compared to 8.4% in fiscal 1995.

For fiscal 1996, capital expenditures totaled \$297 million, which included 27 new supermarkets, 3 new liquor stores, 72 remodels and enlargements and 23 stores which were converted to Food Basics franchised stores in Canada.

For fiscal 1997, the Company has planned capital expenditures of approximately \$310 million and plans to open 40 new supermarkets, remodel and expand 30 stores and open approximately 20 Food Basics franchised stores in Canada. It has been the Company's experience over the past several years that it typically takes 12 to 15 months after opening for a new store to recoup its opening costs and become profitable thereafter. Risks inherent in retail real estate investments are primarily associated with competitive pressures in the marketplace. From fiscal 1997

through fiscal 2000, the Company intends to improve the use of technology through scanning and other technological advances to improve customer service, store operations and merchandising and to intensify advertising and promotions. The Company currently expects to close approximately 53 stores in fiscal year 1997, in addition to 12 stores which will be converted to the Food Basics format in Canada.

The Company plans to open approximately 50 new supermarkets in fiscal 1998 and approximately 50 new supermarkets per year thereafter for several years, with an attendant increase in square footage of approximately 3% per year, and to remodel an average of 50 stores per year. The Company's concentration will be on larger stores in the 50,000 to 65,000 square foot range. Costs of each project will vary significantly based upon size, marketing format, geographic area and development involvement required from the Company. The planned costs of these projects approximate \$4 million for a new store and \$1 million for a remodel or enlargement. Traditionally, the Company leases real estate and expends capital on leasehold improvements and store fixtures and fittings. Consistent with the Company's history, most new store activity will be directed into those areas where the Company achieves its best profitability. Remodeling and enlargement programs are normally undertaken based upon competitive opportunities and usually involve updating a store to a more modern and competitive format.

On March 18, 1997, the Board of Directors increased the Company's quarterly dividend from \$0.05 to \$0.10 per share which will increase the annual dividend payment from \$7.6 million in fiscal 1996 to \$15.3 million in fiscal 1997.

At fiscal year end, the Company's existing senior debt rating was Baa3 with Moody's Investors Service and BB+ with Standard & Poor's Ratings Group. On April 14, 1997, Standard & Poor's Ratings Group upgraded the Company's rating to BBB-. This rating change is not expected to have a material effect on the Company's profitability or availability of credit. A further change in either of these ratings could affect the availability and cost of financing.

The Company's current cash resources, together with cash generated from operations, will be sufficient for the Company's 1997 capital expenditure program, mandatory scheduled debt repayments and dividend payments throughout fiscal 1997.

IMPACT OF NEW ACCOUNTING PRONOUNCEMENT

Effective February 25, 1996, the Company adopted Statement of Financial Accounting Standards No. 123 "Accounting for Stock-Based Compensation" ("SFAS 123"). In conjunction with the adoption, the Company will continue to apply the intrinsic value based method of accounting prescribed by Accounting Principles Board Opinion No. 25 "Accounting for Stock Issued to Employees" with pro forma disclosure of net income and earnings per share as if the fair value based method prescribed by SFAS 123 had been applied.

In February 1997, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 128 "Earnings Per Share" ("SFAS 128"). SFAS 128 simplifies the financial accounting and reporting standards for computing and presenting earnings per share ("EPS") previously found in Accounting Principles Board Opinion No. 15, "Earnings Per Share" and makes them comparable to international EPS standards. SFAS 128 applies to entities with publicly held common stock or common stock equivalents. SFAS 128 replaces the presentation of primary EPS with a presentation of basic EPS. SFAS 128 requires dual presentation of basic and diluted EPS on the face of the income statement for all entities with complex capital structures and requires a reconciliation of the numerator and denominator of the basic EPS computation to the numerator and denominator of the diluted EPS computation.

SFAS 128 is effective for financial statements issued for periods ending after December 15, 1997, including interim periods and requires restatement of all prior period EPS data presented. Earlier application is not permitted. The Company will adopt SFAS 128 in fiscal 1997 and believes the computation of basic EPS will not result in a material difference from primary EPS as currently computed.

Statements of Consolidated Operations

The Great Atlantic & Pacific Tea Company, Inc.

(Dollars in thousands, except per share amounts)	Fiscal 1996	Fiscal 1995	Fiscal 1994
Sales	\$ 10,089,014	\$ 10,101,356	\$ 10,331,950
Cost of merchandise sold	(7,167,315)	(7,166,119)	(7,388,495)
Gross margin	2,921,699	2,935,237	2,943,455
Store operating, general and administrative expense	(2,752,396)	(2,783,503)	(2,873,985)
Write-off of goodwill and long-lived assets	—	—	(127,000)
Income (loss) from operations	169,303	151,734	(57,530)
Interest expense	(73,208)	(73,143)	(72,972)
Interest income	4,496	2,501	1,054
Income (loss) before income taxes and cumulative effect of accounting change	100,591	81,092	(129,448)
Provision for income taxes	(27,559)	(23,868)	(37,138)
Income (loss) before cumulative effect of accounting change	73,032	57,224	(166,586)
Cumulative effect on prior years of change in accounting principle:			
Postemployment benefits	—	—	(4,950)
Net income (loss)	\$ 73,032	\$ 57,224	\$ (171,536)
Earnings (loss) per share:			
Income (loss) before cumulative effect of accounting change	\$ 1.91	\$ 1.50	\$ (4.36)
Cumulative effect on prior years of change in accounting principle:			
Postemployment benefits	—	—	(.13)
Net income (loss) per share	\$ 1.91	\$ 1.50	\$ (4.49)

Statements of Consolidated Shareholders' Equity

The Great Atlantic & Pacific Tea Company, Inc.

(Dollars in thousands, except share amounts)	Fiscal 1996	Fiscal 1995	Fiscal 1994
Common stock:			
Shares:			
Issued and outstanding at beginning of year	38,220,333	38,220,333	38,220,333
Stock options exercised	27,383	—	—
Issued and outstanding at end of year	38,247,716	38,220,333	38,220,333
Balance at beginning of year	\$ 38,220	\$ 38,220	\$ 38,220
Stock options exercised	27	—	—
Balance at end of year	\$ 38,247	\$ 38,220	\$ 38,220
Capital surplus:			
Balance at beginning of year	\$ 453,121	\$ 453,121	\$ 453,121
Stock options exercised	630	—	—
Balance at end of year	\$ 453,751	\$ 453,121	\$ 453,121
Cumulative translation adjustment:			
Balance at beginning of year	\$ (50,936)	\$ (49,227)	\$ (26,103)
Exchange adjustment	1,242	(1,709)	(3,317)
Elimination of deferred income tax asset (see "Income Taxes" footnote)	—	—	(19,807)
Balance at end of year	\$ (49,694)	\$ (50,936)	\$ (49,227)
Retained earnings:			
Balance at beginning of year	\$ 382,380	\$ 332,800	\$ 529,179
Net income (loss)	73,032	57,224	(171,536)
Cash dividends	(7,644)	(7,644)	(24,843)
Balance at end of year	\$ 447,768	\$ 382,380	\$ 332,800

See Notes to Consolidated Financial Statements.

Consolidated Balance Sheets

The Great Atlantic & Pacific Tea Company, Inc.

	February 22, 1997	February 24, 1996
<i>(Dollars in thousands)</i>		
A S S E T S		
<i>Current assets:</i>		
Cash and short-term investments	\$ 98,830	\$ 99,772
Accounts receivable	213,888	205,133
Inventories	881,288	826,510
Prepaid expenses and other assets	37,373	43,520
Total current assets	1,231,379	1,174,935
<i>Property:</i>		
Land	128,779	129,567
Buildings	343,076	321,830
Equipment and leasehold improvements	2,118,808	2,084,609
Total-at cost	2,590,663	2,536,006
Less accumulated depreciation and amortization	(1,104,159)	(1,074,841)
	1,486,504	1,461,165
Property leased under capital leases	103,474	93,379
Property-net	1,589,978	1,554,544
Other assets	181,315	131,368
	<u>\$3,002,672</u>	<u>\$2,860,847</u>
LIABILITIES AND SHAREHOLDERS' EQUITY		
<i>Current liabilities:</i>		
Current portion of long-term debt	\$ 18,290	\$ 13,040
Current portion of obligations under capital leases	12,708	13,125
Accounts payable	468,808	452,257
Book overdrafts	182,305	157,022
Accrued salaries, wages and benefits	146,737	127,133
Accrued taxes	52,269	59,407
Other accruals	134,888	161,984
Total current liabilities	1,016,005	983,968
Long-term debt	701,609	650,169
Obligations under capital leases	137,886	129,887
Deferred income taxes	113,188	120,904
Other non-current liabilities	143,912	153,134
Commitments & contingencies		
<i>Shareholders' equity:</i>		
Preferred stock-no par value; authorized- 3,000,000 shares; issued-none		
Common stock-\$1 par value; authorized - 80,000,000 shares; issued and outstanding 38,247,716 and 38,220,333 shares, respectively	38,247	38,220
Capital surplus	453,751	453,121
Cumulative translation adjustment	(49,694)	(50,936)
Retained earnings	447,768	382,380
Total shareholders' equity	890,072	822,785
	<u>\$3,002,672</u>	<u>\$2,860,847</u>

See Notes to Consolidated Financial Statements.

Statements of Consolidated Cash Flows

The Great Atlantic & Pacific Tea Company, Inc.

(Dollars in thousands)

	Fiscal 1996	Fiscal 1995	Fiscal 1994
Cash Flows From Operating Activities:			
Net income (loss)	\$ 73,032	\$ 57,224	\$ (171,536)
Adjustments to reconcile net income (loss) to cash provided by operating activities:			
Write-off of goodwill and long-lived assets	—	—	127,000
Cumulative effect on prior years of change in accounting principle:			
Postemployment benefits	—	—	4,950
Depreciation and amortization	230,748	225,449	235,444
Deferred income tax provision (benefit) on income (loss)			
before cumulative effect of accounting change	(1,067)	9,496	20,836
(Gain) loss on disposal of owned property	1,338	(3,177)	(816)
(Increase) decrease in receivables	(5,615)	556	(15,197)
(Increase) decrease in inventories	(53,672)	(13,103)	34,048
(Increase) decrease in prepaid expenses and other current assets	6,401	(573)	(1,341)
Increase in other assets	(26,753)	(12,066)	(3,925)
Increase (decrease) in accounts payable	15,950	3,944	(9,996)
Increase (decrease) in accrued expenses	(2,657)	(4,251)	1,295
Increase (decrease) in store closing reserves	(8,600)	(18,240)	2,012
Increase (decrease) in other accruals and other liabilities	(13,307)	16,518	(43,603)
Other operating activities, net	271	193	2,169
Net cash provided by operating activities	216,069	261,970	181,340
Cash Flows From Investing Activities:			
Expenditures for property	(296,878)	(236,139)	(214,886)
Proceeds from disposal of property	19,408	34,576	12,113
Net cash used in investing activities	(277,470)	(201,563)	(202,773)
Cash Flows From Financing Activities:			
Changes in short-term debt	25,903	25,598	(30,912)
Proceeds under revolving lines of credit and long-term borrowings	126,445	594,613	229,447
Payments on revolving lines of credit and long-term borrowings	(96,804)	(683,442)	(93,085)
Principal payments on capital leases	(13,166)	(17,953)	(15,923)
Increase (decrease) in book overdrafts	24,901	(1,075)	(37,720)
Proceeds from stock options exercised	657	—	—
Cash dividends	(7,644)	(7,644)	(24,843)
Net cash provided by (used in) financing activities	60,292	(89,903)	26,964
Effect of exchange rate changes on cash and short-term investments	167	338	(837)
Net Increase (Decrease) in Cash and Short-term Investments	(942)	(29,158)	4,694
Cash and Short-term Investments at Beginning of Year	99,772	128,930	124,236
Cash and Short-term Investments at End of Year	\$ 98,830	\$ 99,772	\$ 128,930

See Notes to Consolidated Financial Statements.

SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation

The consolidated financial statements include the accounts of the Company and all majority-owned subsidiaries. The Company operates retail supermarkets in the United States and Canada. The U.S. operations are mainly in the Eastern part of the U.S. and certain parts of the Midwest. See the following footnotes for additional information on the Canadian Operations: Operations in Geographic Areas, Write-off of Goodwill and Long-Lived Assets, Food Basics Franchise Business, Income Taxes and Retirement Plans and Benefits.

Revenue Recognition

Retail revenue is recognized at point of sale while wholesale revenue is recognized when goods are shipped.

Fiscal Year

The Company's fiscal year ends on the last Saturday in February. Fiscal 1996 ended February 22, 1997, fiscal 1995 ended February 24, 1996 and fiscal 1994 ended February 25, 1995. Fiscal 1996, fiscal 1995 and fiscal 1994 were each comprised of 52 weeks.

Common Stock

The principal shareholder of the Company, Tengelmann Warenhandels-gesellschaft, owned 54.13% of the Company's common stock as of February 22, 1997.

Cash and Short-term Investments

Short-term investments that are highly liquid with an original maturity of three months or less are included in cash and short-term investments and are deemed to be cash equivalents.

Inventories

Store inventories are valued principally at the lower of cost or market with cost determined under the retail method. Warehouse and other inventories are valued primarily at the lower of cost or market with cost determined on a first-in, first-out basis. Inventories of certain acquired companies are valued using the last-in, first-out method, which was their practice prior to acquisition.

Advertising Costs

Advertising costs are expensed as incurred. The Company recorded advertising expense of \$138 million for both fiscal 1996 and 1995, and \$151 million for fiscal 1994.

Properties

Depreciation and amortization are provided on the straight-line basis over the estimated useful lives of the assets. Buildings are depreciated based on lives varying from twenty to fifty years and equipment based on lives varying from three to ten years. Real property leased under capital leases is amortized over the lives of the respective leases or over their economic useful lives, whichever is less. Properties designated for sale are classified as current assets.

Pre-opening Costs

The costs of opening new stores are expensed in the year incurred.

Earnings (Loss) Per Share

Earnings (loss) per share is based on the weighted average number of common and dilutive common equivalent shares outstanding during the fiscal year which was 38,287,589 in fiscal 1996, 38,221,707 in fiscal 1995, and 38,220,333 in fiscal 1994. Stock options outstanding were considered common stock equivalents to the extent that they were dilutive.

In February 1997, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 128 "Earnings Per Share" ("SFAS 128"). The Company will adopt SFAS 128 in fiscal 1997 and believes the computation of basic earnings per share ("EPS") will not result in a material difference from primary EPS as currently computed.

Excess of Cost over Net Assets Acquired

The excess of cost over fair value of net assets acquired is amortized on a straight-line basis over forty years. The Company recorded amortization expense of \$1.5 million for both fiscal 1996 and fiscal 1995, and \$2.6 million for fiscal 1994. The accumulated amortization relating to goodwill amounted to \$10.2 million and \$8.7 million at February 22, 1997 and February 24, 1996, respectively. At each balance sheet date, management reassesses the appropriateness of the goodwill balance based on forecasts of cash flows from operating results on an undiscounted basis. If the results of such comparison indicate that an impairment may exist, the Company will recognize a charge to operations at that time based upon the difference between the present value of the expected cash flows from future operating results (utilizing a discount rate equal to the Company's average cost of funds at that time) and the balance sheet value. The recoverability of goodwill is at risk to the extent the Company is unable to achieve its forecast assumptions regarding cash flows from operating results. At February 22, 1997, the Company estimates that the cash flows projected to be generated by the respective businesses on an undiscounted basis should be sufficient to recover the existing goodwill balance over its remaining life (see "Write-off of Goodwill and Long-Lived Assets" footnote).

Long-Lived Assets

The Company adopted the provisions of Statement of Financial Accounting Standards No. 121 "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to be Disposed of" ("SFAS 121") during the fourth quarter of fiscal 1995. SFAS 121 establishes accounting standards for the impairment of long-lived assets, certain identifiable intangibles, and goodwill related to those assets to be held and used and for long-lived assets and certain identifiable intangibles to be disposed of. The Company reviews the carrying values of its long-lived and identifiable intangible assets for possible impairment whenever events or changes in circumstances indicate that the carrying amount of assets may not be recoverable.

Such review is based upon groups of assets and the undiscounted estimated future cash flows from such assets to determine if the carrying value of such assets are recoverable from their respective cash flows. The adoption of SFAS No. 121 did not have an effect on the financial position or results of operations of the Company.

Income Taxes

The Company provides deferred income taxes on temporary differences between amounts of assets and liabilities for financial reporting purposes and such amounts as measured by tax laws.

Current Liabilities

Certain accounts payable checks issued but not presented to banks frequently result in negative balances for accounting purposes. Such amounts are classified as "Book overdrafts" in the accompanying balance sheets.

The Company accrues for vested and non-vested vacation pay. Liabilities for compensated absences of \$79 million and \$80 million at

February 22, 1997 and February 24, 1996, respectively, are included in the balance sheet caption "Accrued salaries, wages and benefits."

Stock-Based Compensation

Effective February 25, 1996, the Company adopted Statement of Financial Accounting Standards No. 123 "Accounting for Stock-Based Compensation" ("SFAS 123"). In conjunction with the adoption, the Company will continue to apply the intrinsic value based method of accounting prescribed by Accounting Principles Board Opinion No. 25 "Accounting for Stock Issued to Employees" with pro forma disclosure of net income and earnings per share as if the fair value based method prescribed by SFAS 123 had been applied.

Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

The accompanying balance sheets include liabilities with respect to self-insured workers' compensation and general liability claims. The Company determines the required liability of such claims based upon various assumptions which include, but are not limited to, the Company's historical loss experience, industry loss standards, projected loss development factors, projected payroll, employee headcount and other internal data. It is reasonably possible that the final resolution of some of these claims may require significant expenditures by the Company in excess of its existing reserves, over an extended period of time and in a range of amounts that cannot be reasonably estimated.

Reclassifications

Certain reclassifications have been made to the prior years' financial statements in order to conform to the current year's presentation.

INVENTORY

Approximately 27.0% of the Company's inventories are valued using the last-in, first-out ("LIFO") method. Such inventories would have been \$15 million and \$14 million higher at February 22, 1997 and February 24, 1996, respectively, if the retail and first-in, first-out methods were used. During fiscal 1996 and fiscal 1995, the Company recorded a LIFO charge of approximately \$1 million and \$2 million, respectively. During fiscal 1994, the Company recorded a LIFO credit of approximately \$2 million. Liquidation of LIFO layers in the periods reported did not have a significant effect on the results of operations.

FOOD BASICS FRANCHISE BUSINESS

As of February 22, 1997, the Company serviced 49 Food Basics franchised stores. During fiscal 1996, the Company had wholesale sales of \$205 million to these franchised stores. A majority of the Food Basics franchised stores were converted from Company operated supermarkets. The Company subleases the stores to the franchisees and provides them with equipment and inventory (see "Lease Obligations" footnote).

Included in other assets are Food Basics franchised business receivables, net of allowance for doubtful accounts, amounting to \$40.2 million as of February 22, 1997 and \$1.6 million as of February 24, 1996. The receivables are related to the initial inventory notes and equipment leases. The inventory notes are collateralized by the inventory in the stores, while the equipment lease receivables are collateralized by the equipment in the stores. The allowance for doubtful accounts is recorded to the extent of the franchisee's net operating losses. The current portion of the inventory and equipment leases of approximately \$2.4 million as of February 22, 1997 and \$0.1 million as of February 24, 1996 are included in accounts receivable.

Included below are the amounts due to the Company for the next five years and thereafter from the franchised stores for equipment leases and inventory notes.

<i>(Dollars in thousands)</i>	
1997	\$ 5,761
1998	6,598
1999	6,598
2000	6,598
2001	6,598
2002 and thereafter	25,536
	57,689
Less interest portion	(15,040)
Due from Food Basics franchise business	\$ 42,649

Approximately \$34 million of the above notes relate to equipment leases which were non-cash transactions and accordingly, have been excluded from the consolidated statement of cash flows.

WRITE-OFF OF GOODWILL AND LONG-LIVED ASSETS

During the third quarter of fiscal 1994, the Company recorded a non-cash charge of \$127 million reflecting \$50 million for the write-off of goodwill related to the acquisition of Miracle Food Mart ("Miracle") stores in Canada and \$77 million for the write-down of certain Miracle fixed assets. Miracle experienced a work stoppage for a 14-week period at the end of fiscal 1993. Under Canadian labor laws the stores were closed during this time period. The labor dispute was settled and the stores re-opened for business on February 25, 1994. The Company anticipated that the new labor agreement would have a positive impact on operating results assuming historical sales levels could be attained. Through the first half of fiscal 1994, the Company expended significant promotional efforts in order to regain its pre-strike sales levels. The sales performance through the first half of fiscal 1994 was disappointing and the Company continued to monitor Miracle's performance through the third quarter. Sales performance in the third quarter of fiscal 1994 continued to be negative when compared to pre-strike sales levels. The Company, no longer believing that Miracle's negative operating performance was temporary, revised its future expected cash flow projections. These revised projections indicated that the goodwill balance would not be recoverable over its remaining life. Further, these projections indicated that the operating results of Miracle would not be sufficient to absorb the depreciation and amortization of certain of its operating fixed assets. Accordingly, Miracle's goodwill balance was written-off and fixed assets relating to Miracle stores which were expected to continue to generate operating losses were written-down as of the end of the third quarter of fiscal 1994.

INDEBTEDNESS

Debt consists of:

(Dollars in thousands)	February 22, 1997	February 24, 1996
9 1/8% Notes, due January 15, 1998	\$200,000	\$200,000
7.70% Senior Notes, due January 15, 2004	200,000	200,000
7.78% Notes, due November 1, 2000	75,000	75,000
Mortgages and Other Notes, due 1997 through 2014 (average interest rates at year end of 9.35% and 9.77%, respectively)	38,878	39,279
U.S. Bank Borrowings at 5.76% and 5.73%, respectively	147,000	95,000
Canadian Commercial Paper at 3.44% and 6.20%, respectively	2,192	7,977
Canadian Bank Borrowings at 3.65% and 6.03%, respectively	56,956	46,223
Less unamortized discount on 9 1/8% Notes	(127)	(270)
	719,399	663,209
Less current portion	(18,290)	(13,040)
Long-term debt	\$701,609	\$650,169

In December 1995, the Company executed an unsecured five year \$400 million U.S. credit agreement and a five year C\$100 million (U.S. \$73 million as of February 22, 1997) Canadian credit agreement with a syndicate of banks enabling it to borrow funds on a revolving basis sufficient to refinance any outstanding short-term borrowings. The Company pays a facility fee ranging from 3/16% to 1/2% per annum on the U.S. and Canadian revolving credit facilities. Borrowings under the U.S. revolving credit agreement were \$95 million and \$60 million at February 22, 1997 and February 24, 1996, respectively. A&P Canada has outstanding borrowings of \$59 million and \$54 million at February 22, 1997 and February 24, 1996, respectively. As of February 22, 1997, the Company has available \$305 million under its U.S. revolver and C\$19 million (U.S. \$14 million at February 22, 1997) under the Canadian credit agreement. As of February 24, 1996, the Company had available \$340 million under its U.S. revolver and C\$22 million (U.S. \$16 million at February 24, 1996) under the Canadian credit agreement. In addition, the U.S. has uncommitted lines of credit with various banks amounting to \$145 million and \$50 million as of February 22, 1997 and February 24, 1996, respectively. Borrowings under these uncommitted lines of credit amounted to \$52 million and \$35 million as of February 22, 1997 and February 24, 1996, respectively.

As of February 22, 1997, the Company has outstanding a total of \$400 million of unsecured, non-callable public debt securities in the form of \$200 million 9 1/8% Notes due January 15, 1998, and \$200 million 7.70% Notes due January 15, 2004. As of February 22, 1997, the Company has \$305 million available under the U.S. five year \$400 million revolving credit facility, accordingly, the \$200 million 9 1/8% Notes due January 15, 1998 are recorded as non-current since the Company has the ability and intent to refinance these Notes on a long-term basis.

On April 15, 1997, the Company issued \$300 million 7.75% 10 year Notes due April 15, 2007. The Company used the net proceeds

to reduce bank borrowings under the U.S. and Canadian revolving credit facilities, prepay other indebtedness and for general corporate purposes. After reducing borrowings under the U.S. and Canadian revolving credit facilities with the net proceeds of the \$300 million Notes, the Company currently intends to draw upon the funds available under the U.S. credit facility to repay at maturity indebtedness owing in respect of the Company's 9 1/8% Notes due January 15, 1998.

During April 1997 the Company began discussions with its lenders under its U.S. and Canadian revolving credit facilities (the "Facility") to amend such Facility to principally (i) extend the maturity; (ii) lower the cost of borrowing by reducing the spread payable over certain reference rates; and (iii) reduce the facility fees payable thereunder. Although there is no assurance that the Facility will be amended, the Company does expect to obtain such an amendment.

On October 17, 1995, the Company's Canadian subsidiary, The Great Atlantic & Pacific Company of Canada, Ltd. ("A&P Canada"), issued U.S. \$75 million of unsecured, non-callable 7.78% Notes due November 1, 2000 guaranteed by the Company. The net proceeds from the issuance of these Notes were used to repay indebtedness under the Canadian subsidiary's revolving credit facility. In conjunction with the issuance of the U.S. \$75 million Notes, A&P Canada entered into a five year cross-currency swap agreement expiring November 1, 2000. The cross-currency swap agreement requires A&P Canada to make net payments to the counterparty based on a fixed interest differential on a semi-annual basis. The interest differential to be paid under the swap agreement is accrued over the life of the agreement as an adjustment to the yield of the 7.78% Notes and is recorded as interest expense. The Company is exposed to credit losses in the event of nonperformance by the counterparty to its currency swap. However, the Company anticipates that the counterparty will be able to fully satisfy its obligations under the contracts.

The Company's loan agreements and certain of its notes contain various financial covenants which require, among other things, minimum net worth and maximum levels of indebtedness and lease commitments. The Company was in compliance with all such financial covenants as of February 22, 1997 and believes that it will continue to be in compliance.

The net book value of real estate pledged as collateral for all mortgage loans amounted to approximately \$48 million and \$49 million as of February 22, 1997 and February 24, 1996, respectively.

Combined U.S. bank and Canadian bank and commercial paper borrowings of \$196 million as of February 22, 1997 are classified as non-current as the Company has the ability and intent to refinance these borrowings on a long-term basis.

Maturities for the next five fiscal years and thereafter are: 1997-\$218 million (\$200 million of which is expected to be refinanced); 1998-\$40 million; 1999-\$54 million; 2000-\$194 million; 2001-\$3 million; 2002 and thereafter - \$211 million. Interest payments on indebtedness were approximately \$49 million for fiscal 1996, \$54 million for fiscal 1995 and \$52 million for fiscal 1994.

FAIR VALUE OF FINANCIAL INSTRUMENTS

The estimated fair values of the Company's financial instruments are as follows:

<i>(Dollars in thousands)</i>	February 22, 1997		February 24, 1996	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Liabilities:				
9 1/8% Notes, due				
January 15, 1998	\$199,873	\$204,296	\$199,730	\$209,440
7.70% Senior Notes, due				
January 15, 2004	\$200,000	\$203,390	\$200,000	\$198,360
7.78% Notes, due				
November 1, 2000	\$ 75,000	\$ 76,912	\$ 75,000	\$ 75,713
Total Indebtedness	\$719,899	\$729,624	\$663,209	\$671,992

Fair value for the public debt securities is based on quoted market prices. With respect to all other indebtedness, Company management has evaluated such debt instruments and has determined, based on interest rates and terms, that the fair value of such indebtedness approximates carrying value at February 22, 1997 and February 24, 1996. As of February 22, 1997 and February 24, 1996, the carrying values of cash and short-term investments, accounts receivable and accounts payable approximated fair values due to the short-term maturities of these instruments.

At February 22, 1997, the fair value of the cross-currency swap agreement was unfavorable by approximately \$5 million. The fair value was determined by the counterparty which is a widely recognized investment banker.

As of the end of fiscal 1996, the Company holds equity securities of both common and cumulative preferred stock in Isosceles PLC which were written-off in their entirety during fiscal 1992. There are no quoted market prices for these securities and it is not practicable, considering the materiality of these securities to the Company, to obtain an estimate of their fair value. The Company believes that the fair value for these securities is zero based upon Isosceles' current and prior year's results.

LEASE OBLIGATIONS

The Company operates primarily in leased facilities. Lease terms generally range up to twenty-five years for store leases and thirty years for other leased facilities, with options to renew for additional periods. The majority of the leases contain escalation clauses relating to real estate tax increases and certain store leases provide for increases in rentals when sales exceed specified levels. In addition, the Company also leases some store equipment and trucks.

The consolidated balance sheets include the following:

<i>(Dollars in thousands)</i>	February 22, 1997	February 24, 1996
Real property leased under capital leases	\$ 223,507	\$ 206,543
Accumulated amortization	(120,033)	(113,164)
	\$ 103,474	\$ 93,379

The Company entered into \$22 million of new capital leases during fiscal 1996. These capital lease amounts are non-cash transactions and, accordingly, have been excluded from the consolidated statement of cash flows. The Company did not enter into any new capital leases during fiscal 1995 or 1994. Interest paid as part of capital lease obligations was approximately \$17, \$18 and \$20 million in fiscal 1996, 1995 and 1994, respectively.

Rent expense for operating leases consists of:

<i>(Dollars in thousands)</i>	Fiscal 1996	Fiscal 1995	Fiscal 1994
Minimum rentals	\$162,752	\$ 154,439	\$154,488
Contingent rentals	5,383	5,890	6,619
	\$168,135	\$ 160,329	\$161,107

Future minimum annual lease payments for capital leases and noncancelable operating leases in effect at February 22, 1997 are shown in the table below. All amounts are exclusive of lease obligations and sublease rentals applicable to facilities for which reserves have previously been established. In addition, the Company subleases 49 stores to the Food Basics franchise business. Included in the operating lease table below are the rental payments made by the Company offset by the rental income received from the Food Basics franchised stores.

<i>(Dollars in thousands)</i>	Capital Leases Real Property	Operating Leases
Fiscal		
1997	\$ 29,602	\$ 170,833
1998	28,318	157,382
1999	26,231	146,533
2000	25,120	134,677
2001	23,964	133,939
2002 and thereafter	153,393	1,241,453
	286,628	\$1,984,817
Less executory costs	(2,149)	
Net minimum rentals	284,479	
Less interest portion	(133,885)	
Present value of net minimum rentals	\$ 150,594	

INCOME TAXES

The components of income (loss) before income taxes and cumulative effect of accounting change are as follows:

<i>(Dollars in thousands)</i>	Fiscal 1996	Fiscal 1995	Fiscal 1994
United States	\$ 68,478	\$73,364	\$ 80,509
Canadian	32,113	7,728	(209,957)
Total	\$100,591	\$81,092	\$(129,448)

The provision for income taxes before cumulative effect of accounting change consists of the following:

<i>(Dollars in thousands)</i>	Fiscal 1996	Fiscal 1995	Fiscal 1994
Current:			
Federal	\$ 24,228	\$ 15,129	\$ 8,577
Canadian	700	(5,622)	2,687
State and local	3,693	4,865	5,038
	28,626	14,372	16,302
Deferred:			
Federal	(926)	9,387	(9,922)
Canadian	14,329	3,448	(88,943)
State and local	(141)	109	114
Canadian valuation allowance	(14,329)	(3,448)	119,592
	(1,067)	9,496	20,836
	\$ 27,559	\$ 23,868	\$ 37,138

The deferred income tax provision (benefit) results primarily from the annual change in temporary differences between amounts of assets and liabilities for financial reporting purposes and such amounts as measured by tax laws, Canadian net operating tax loss carryforwards and the Canadian valuation allowance.

Notes to Consolidated Financial Statements, Continued

The Canadian deferred income tax benefit for fiscal 1994 relates primarily to net operating tax loss carryforwards, the write-off of goodwill and certain long-lived assets and other temporary differences associated with the Company's operations in Canada. Management assessed the likelihood of realizing the Canadian net deferred income tax assets and, based on all available evidence, concluded that it was not likely that such assets would be realized. Accordingly, during the third quarter of fiscal 1994, the Company recorded a valuation allowance to reserve for previously recognized deferred tax benefits and continued through the remainder of fiscal 1994 to provide a valuation allowance against its deferred income tax benefits.

During fiscal 1996 and fiscal 1995, the Company has reduced the income tax valuation allowance to the extent the Canadian operations have been able to generate taxable income, however, the Company was unable to conclude that it was more likely than not that the remaining deferred tax assets would be realized. This conclusion was based in part on the competitive Canadian marketplace and the significant losses experienced prior to fiscal 1995. Accordingly, at February 22, 1997 the Company is continuing to fully reserve its Canadian net deferred tax assets. The valuation allowance will be adjusted when and if, in the opinion of Management, significant positive evidence exists which indicates that it is more likely than not that the Company will be able to realize the Canadian deferred tax assets.

The Company historically provided U.S. deferred taxes on the undistributed earnings of the Canadian operations. During fiscal 1994, the Company made an election to permanently reinvest prior years' earnings and, accordingly, reversed deferred tax liabilities of \$27 million associated with the undistributed earnings of the Canadian operations. Further, in conjunction with this decision, the Company recorded a direct charge to equity of approximately \$20 million to eliminate the deferred tax asset related to the Cumulative Translation Adjustment.

The Company's Canadian net operating tax loss carryforwards of approximately \$180.4 million will expire between February 1999 and February 2003.

A reconciliation of income taxes at the 35% federal statutory income tax rate for fiscal 1996, 1995 and 1994 to income taxes as reported is as follows:

(Dollars in thousands)	Fiscal 1996	Fiscal 1995	Fiscal 1994
Income taxes computed at federal			
statutory income tax rate	\$ 35,207	\$ 28,382	\$ (45,307)
Targeted jobs tax credits	-	-	(1,300)
State and local income taxes, net of			
federal tax benefit	2,312	3,233	3,348
Tax rate differential relating			
to Canadian operations	3,789	(4,879)	(12,775)
Canadian valuation allowance	(14,329)	(3,448)	119,592
Goodwill	580	580	580
Reduction of tax liabilities			
associated with undistributed			
earnings	-	-	(27,000)
Income taxes, as reported	\$ 27,559	\$ 23,868	\$ 37,138

The fiscal 1995 tax rate differential relating to Canadian operations in the above table includes a \$6.5 million benefit related to a refund of previously paid Canadian taxes.

Income tax payments, net of refunds, for fiscal 1996, 1995 and 1994 were approximately \$13, \$19 and \$12 million, respectively.

The components of net deferred tax assets (liabilities) are as follows:

(Dollars in thousands)	February 22, 1997	February 24, 1996
Current assets:		
Insurance reserves	\$ 24,186	\$ 27,372
Other reserves	3,524	8,172
Lease obligations	1,817	1,994
Pension obligations	2,390	1,970
Miscellaneous	9,079	4,968
	40,996	44,476
Current liabilities:		
Inventories	(14,819)	(15,172)
Health and Welfare	(9,534)	(10,007)
Miscellaneous	(5,997)	(2,678)
	(30,350)	(27,857)
Valuation allowance	(3,337)	(2,660)
Deferred income taxes included in		
prepaid expenses and other assets	\$ 7,309	\$ 13,959
Non-current assets:		
Isosceles investment	\$ 42,617	\$ 42,617
Fixed assets	4,061	10,129
Other reserves	5,420	7,191
Lease obligations	19,166	20,519
Canadian loss carryforwards	80,494	85,494
Insurance reserves	6,720	8,820
Accrued postretirement and		
postemployment benefits	28,110	28,569
Pension obligations	6,300	6,300
Miscellaneous	18,302	17,727
	211,190	227,366
Non-current liabilities:		
Fixed assets	(177,636)	(193,432)
Pension obligations	(21,050)	(17,752)
Miscellaneous	(29,453)	(25,800)
	(228,139)	(236,984)
Valuation allowance	(96,239)	(111,286)
Deferred income taxes	\$ (113,188)	\$ (120,904)

RETIREMENT PLANS AND BENEFITS

Defined Benefit Plans

The Company provides retirement benefits to certain non-union and some union employees under various defined benefit plans. The Company's defined benefit pension plans are non-contributory and benefits under these plans are generally determined based upon years of service and, for salaried employees, compensation. The Company funds these plans in amounts consistent with the statutory funding requirements.

The components of net pension cost are as follows:

(Dollars in thousands)	Fiscal 1996	Fiscal 1995	Fiscal 1994
Service cost	\$ 10,826	\$ 9,340	\$ 11,182
Interest cost	24,798	23,976	22,858
Actual return on plan assets	(34,921)	(42,724)	(17,448)
Net amortization and deferral	5,254	16,362	(9,246)
Net pension cost	\$ 5,957	\$ 6,954	\$ 7,346

The Company's defined benefit pension plans are accounted for on a calendar year basis. The majority of plan assets is invested in listed stocks and bonds. The funded status of the plans is as follows:

(Dollars in thousands)	1996		1995	
	Assets Exceed Accumulated Benefits	Accumulated Benefits Exceed Assets	Assets Exceed Accumulated Benefits	Accumulated Benefits Exceed Assets
Accumulated benefit obligation:				
Vested	\$300,111	\$ 38,726	\$267,391	\$ 36,396
Nonvested	3,766	1,907	3,393	1,776
	\$303,877	\$ 40,633	\$270,784	\$ 38,172
Projected benefit obligation	\$312,762	\$ 42,969	\$279,667	\$ 40,324
Plan assets at fair value	378,903	22,600	333,100	16,752
Excess (deficiency) of assets over projected benefit obligation	66,141	(20,369)	53,433	(23,572)
Unrecognized net transition (asset) obligation	(7,446)	483	(8,097)	(78)
Unrecognized net (gain) loss from experience differences	(15,059)	(1,109)	(9,271)	2,649
Unrecognized prior service cost	3,082	3,964	3,357	4,115
Additional minimum liability	-	(2,824)	-	(4,614)
Prepaid pension asset (pension liability)	\$ 46,718	\$(19,855)	\$ 39,422	\$(21,500)

The prepaid pension asset is included in other assets while the pension liability is included in accrued salaries, wages and benefits and other non-current liabilities.

During the year ended February 25, 1995, the Company's Canadian subsidiary and the United Food & Commercial Workers International Union, Locals 175 and 633, entered into an agreement which will result in the amalgamation of three of the Company's Canadian defined benefit pension plans with the Canadian Commercial Workers Industry Pension Plan ("CCWIPP"), retroactive to July 1, 1994, subject to the approval of the CCWIPP trustees and the appropriate regulatory bodies. Under the terms of this agreement, CCWIPP will assume the assets and defined benefit liabilities of the three pension plans and the Company will be required to make defined contributions to CCWIPP based upon hours worked by employees who are members of CCWIPP. The Company expects that the necessary approvals will be received by December 1997. The transfer to CCWIPP has been delayed for the past two years as the regulatory bodies have taken longer to review the transfer than originally anticipated. The Company will not change the reporting for these three plans until such approval is received. Accordingly, at February 22, 1997 and February 24, 1996, prepaid pension assets of approximately \$15 million and \$13 million, respectively, related to the aforementioned plans are included in the above table.

Actuarial assumptions used to determine year-end plan status are as follows:

	1996		1995	
	U.S.	Canada	U.S.	Canada
Discount rate	7.50%	7.75%	7.00%	8.50%
Weighted average rate of compensation increase	4.50%	4.00%	4.00%	4.00%
Expected long-term rate of return on plan assets	8.50%	8.80%	8.00%	8.80%

The impact of the changes in the actuarial assumptions has been reflected in the funded status of the pension plans and the Company believes that such changes will not have a material effect on net pension cost for fiscal 1997.

Defined Contribution Plans

The Company maintains a defined contribution retirement plan to which the Company contributes an amount equal to 4% of eligible participants' salaries and a savings plan to which eligible participants may contribute a percentage of eligible salary. The Company contributes to the savings plan based on specified percentages of the participants' eligible contributions. Participants become fully vested in the Company's contributions after 5 years of service. The Company's contributions charged to operations for both plans were approximately \$11 million in each of the three fiscal years in the period ended February 22, 1997.

The Company participates in various multi-employer union pension plans which are administered jointly by management and union representatives and which sponsor most full-time and certain part-time union employees who are not covered by the Company's other pension plans. The pension expense for these plans approximated \$38 million in both fiscal 1996 and 1995, and \$39 million in fiscal 1994. The Company could, under certain circumstances, be liable for unfunded vested benefits or other expenses of jointly administered union/management plans. At this time, the Company has not established any liabilities because such withdrawal from these plans is not probable.

Postretirement Benefits

The Company and its wholly-owned subsidiaries provide postretirement health care and life benefits to certain union and non-union employees. The Company recognizes the cost of providing postretirement benefits during employees' active service period.

The components of net postretirement benefits cost are as follows:

(Dollars in thousands)	Fiscal 1996	Fiscal 1995	Fiscal 1994
Service cost	\$ 794	\$ 600	\$ 600
Interest cost	2,394	2,900	3,600
Net amortization and deferral	(1,100)	(800)	-
Net postretirement benefits cost	\$ 2,088	\$ 2,700	\$ 4,200

The unfunded status of the plans is as follows:

(Dollars in thousands)	Fiscal 1996	Fiscal 1995
Unfunded accumulated benefit obligation:		
Retirees	\$ 17,680	\$ 19,100
Fully eligible active plan participants	4,026	3,500
Other active plan participants	13,225	13,200
	34,931	35,800
Unrecognized net gain from experience differences	16,407	15,600
Accrued postretirement costs	\$ 51,338	\$ 51,400
Assumed discount rate	7.5%	7.0%

The assumed rate of future increase in health care benefit cost was 9.75% in fiscal 1996 and is expected to decline to 5.0% by the year 2020 and remain at that level thereafter. The effect of a one-percentage-point increase in the assumed health care cost trend rate for each future year on the net postretirement health care cost and the accumulated postretirement benefit obligation would be \$0.5 million and \$3.2 million, respectively.

Postemployment Benefits

Effective February 27, 1994, the Company adopted Statement of Financial Accounting Standards No. 112 "Employers' Accounting for Postemployment Benefits" ("SFAS 112"). SFAS 112 requires the accrual of costs for preretirement postemployment benefits provided to former or inactive employees and the recognition of an obligation for these benefits.

The Company's previous accounting policy had been to accrue for workers' compensation and a principal portion of long-term disability benefits and to expense other postemployment benefits, such as short-term disability, as incurred. As a result of adopting SFAS 112, the Company recorded a charge of \$5.0 million, net of applicable income taxes of \$3.9 million, as the cumulative effect of recording the obligation as of the beginning of fiscal 1994. The effect of adopting SFAS 112 had an immaterial effect on the financial results before the cumulative effect of accounting change for fiscal 1994. Further, the costs incurred for fiscal 1996 and fiscal 1995 were not significant.

STOCK OPTIONS

Effective February 25, 1996, the Company adopted SFAS 123 which establishes financial accounting and reporting standards for stock-based employee compensation plans. SFAS 123 encourages all entities to adopt a fair value based method of accounting for stock-based compensation plans in which compensation cost is measured at the date the award is granted based on the fair value of the award and is recognized over the employees' service period. However, SFAS 123 allows an entity to continue to use the intrinsic value based method prescribed by Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees" ("APB 25"), with pro forma disclosures of net income and earnings per share as if the fair value based method had been applied. APB 25 requires compensation expense to be recognized over the employees' service period based on the excess, if any, of the quoted market price of the stock at the date the award is granted or other measurement date, as applicable, over an amount an employee must pay to acquire the stock.

At February 22, 1997, the Company has three fixed stock-based compensation plans. The Company applies the principles of APB 25 for stock options and FASB Interpretation No. 28 for stock appreciation rights ("SAR's"). Most of the options vest over a four year period on the anniversary date of issuance, while some options vest immediately.

The 1994 Stock Option Plan for officers and key employees provides for the granting of 1,500,000 shares as either options or SAR's. Options and SAR's issued under this plan are granted at the fair market value of the Company's common stock at the date of grant. The 1984 Stock Option Plan for officers and key employees, which expired on February 1, 1994, provided for the granting of 1,500,000 shares and was amended as of July 10, 1990 to increase by 1,500,000 the number of options available for grant as either options or SAR's. Each option was available for grant at the fair market value of the Company's common stock on the date the option was granted. SAR's allow the holder, in lieu of purchasing stock, to receive cash in an amount equal to the excess of the fair market value of common stock on the date of exercise over the option price. A total of 65,000 options and 86,500 SAR's was granted in fiscal 1996 under this plan.

The 1994 Stock Option Plan for Board of Directors provides for the granting of 100,000 stock options at the fair market value of the Company's common stock at the date of grant. Options granted under this plan in fiscal 1996, fiscal 1995 and fiscal 1994 totaled 5,200, 1,800 and 19,800, respectively.

The fair value of the fiscal 1996 and 1995 option grants was estimated on the date of grant using the Black-Scholes option-pricing model with the following assumptions: Fiscal 1996 and fiscal 1995; expected volatility of 30%, expected life of 7 years and dividend yield between 0.72% and 0.91%. The risk-free interest rates used for the grants are between 5.57% and 6.94%.

The Company recognized compensation expense of \$5.8 million in fiscal 1996, \$0.3 million for fiscal 1995 and no expense for fiscal 1994 with respect to SAR's. There was no compensation expense recognized for the other fixed plans since the exercise price of the stock options equalled the fair market value of the Company's common stock on the date of grant. Had compensation cost for the Company's stock options been determined based on the fair value at the grant dates for awards under those plans consistent with the fair value methods prescribed by SFAS 123, the Company's net income and earnings per share would have been reduced to the pro forma amounts indicated below:

<i>(Dollars in thousands, except per share amounts)</i>		
	Fiscal 1996	Fiscal 1995
Net Income:		
As reported	\$73,032	\$57,224
Pro forma	\$71,920	\$56,624
Earnings Per Share:		
As reported	\$1.91	\$1.50
Pro forma	\$1.88	\$1.48

A summary of option transactions is as follows:

<i>Officers, Key Employees and Board of Directors</i>	Shares	Weighted Average Exercise Price
Outstanding February 26, 1994	15,000	\$27.63
Granted	69,800	24.22
Outstanding February 25, 1995	84,800	\$24.82
Granted	670,800	27.71
Cancelled or expired	(10,000)	27.88
Outstanding February 24, 1996	745,600	\$27.38
Granted	70,200	27.72
Cancelled or expired	(63,350)	26.13
Exercised	(27,383)	23.85
Outstanding February 22, 1997	725,067	\$27.66
Exercisable at:		
February 24, 1996	34,100	\$25.81
February 22, 1997	182,400	\$27.58
Weighted average fair value of options granted during the year:		
February 24, 1996		\$11.45
February 22, 1997		\$11.94

A summary of stock options outstanding and exercisable at February 22, 1997 is as follows:

Options Outstanding				Options Exercisable	
Range Of Exercise Prices	Number Outstanding at Feb. 22, 1997	Weighted Average Remaining Contractual Life	Weighted Average Exercise Price	Number Exercisable at Feb. 22, 1997	Weighted Average Exercise Price
\$21.50 - \$25.88	26,466	8.5 years	\$23.37	7,183	\$23.22
\$26.50 - \$30.75	89,601	8.9 years	\$27.47	12,467	\$26.55
\$27.63	15,000	4.8 years	\$27.63	15,000	\$27.63
\$27.88	594,000	8.3 years	\$27.88	147,750	\$27.88
	<u>725,067</u>			<u>182,400</u>	

A summary of SAR transactions is as follows:

<i>Officers and Key Employees</i>	Shares	Price Range Per Share
Outstanding February 26, 1994	2,414,125	\$21.50 - \$65.13
Cancelled or expired	(26,500)	39.75 - 59.00
Exercised	(2,500)	23.38
Outstanding February 25, 1995	2,385,125	\$21.50 - \$65.13
Granted	10,000	21.88
Cancelled or expired	(166,750)	23.38 - 46.38
Exercised	(75,625)	21.50 - 24.75
Outstanding February 24, 1996	2,152,750	\$21.50 - \$65.13
Granted	86,500	27.25 - 31.63
Cancelled or expired	(20,000)	27.38 - 56.13
Exercised	(247,237)	21.50 - 34.75
Outstanding February 22, 1997	1,972,013	\$23.00 - \$65.13
Exercisable at:		
February 24, 1996	1,666,500	\$21.50 - \$65.13
February 22, 1997	1,647,388	\$23.00 - \$65.13

LITIGATION

The Company is involved in various claims, administrative agency proceedings and lawsuits arising out of the normal conduct of its business. Although the ultimate outcome of these legal proceedings cannot be predicted with certainty, the management of the Company believes that the resulting liability, if any, will not have a material effect upon the Company's consolidated financial statements or liquidity.

SUMMARY OF QUARTERLY RESULTS (unaudited)

The table below summarizes the Company's results of operations by quarter for fiscal 1996 and 1995. The first quarter of each fiscal year contains sixteen weeks while the other quarters each contain twelve weeks.

<i>(Dollars in thousands, except per share data)</i>	First Quarter	Second Quarter	Third Quarter	Fourth Quarter	Total Year
1996					
Sales	\$3,092,554	\$2,329,987	\$2,318,762	\$2,347,711	\$10,089,014
Gross margin	896,780	662,355	668,664	693,900	2,921,699
Depreciation and amortization	69,558	53,240	53,939	54,011	230,748
Income from operations	52,743	34,553	34,398	47,609	169,303
Interest expense	21,550	16,387	17,028	18,243	73,208
Net income	21,879	13,994	14,091	23,068	73,032
Per share data:					
Net income	.57	.37	.37	.60	1.91
Cash dividends	.05	.05	.05	.05	.20
Market price:					
High	36.750	34.625	34.000	34.375	
Low	22.125	25.875	25.125	29.875	
Number of stores at end of period	993	977	974	973	
Number of franchised stores served at end of period	24	36	47	49	
1995					
Sales	\$3,135,514	\$2,341,171	\$2,293,597	\$2,331,074	\$10,101,356
Gross margin	909,812	669,103	666,121	690,201	2,935,237
Depreciation and amortization	70,400	52,340	51,957	50,752	225,449
Income from operations	46,884	29,861	29,235	45,754	151,734
Interest expense	22,873	16,197	17,159	16,914	73,143
Net income	14,550	9,384	7,735	25,555	57,224
Per share data:					
Net income	.38	.25	.20	.67	1.50
Cash dividends	.05	.05	.05	.05	.20
Market price:					
High	26.250	28.625	28.875	24.875	
Low	19.000	23.875	20.000	19.500	
Number of stores at end of period	1,082	1,063	1,043	1,014	
Number of franchised stores served at end of period	-	-	-	7	

OPERATIONS IN GEOGRAPHIC AREAS

The Company has been engaged in the retail food business since 1859 and currently does business principally under the names A&P, Waldbaum's, Food Emporium, Super Fresh, Farmer Jack, Kohl's, Sav-A-Center, Dominion, and Food Basics. Sales in the table below reflect sales to unaffiliated customers in the United States and Canada as well as wholesale sales to franchised stores.

<i>(Dollars in thousands)</i>	Fiscal 1996	Fiscal 1995	Fiscal 1994
Sales:			
United States	\$ 8,281,925	\$ 8,365,327	\$ 8,540,871
Foreign	1,807,089	1,736,029	1,791,079
Total	\$10,089,014	\$10,101,356	\$10,331,950
Income (Loss) From Operations:			
United States	\$ 122,159	\$ 125,118	\$ 137,804
Foreign	47,144	26,616	(195,334)
Total	\$ 169,303	\$ 151,734	\$ (57,530)

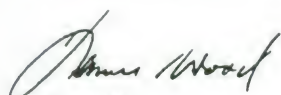
Assets:

United States	\$ 2,549,500	\$ 2,438,353	\$ 2,482,108
Foreign	453,172	422,494	412,680
Total	\$ 3,002,672	\$ 2,860,847	\$ 2,894,788

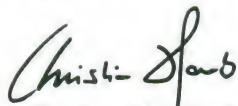
Management's Report on Financial Statements

The management of The Great Atlantic & Pacific Tea Company, Inc. has prepared the consolidated financial statements and related financial data contained in this Annual Report. The financial statements were prepared in accordance with generally accepted accounting principles appropriate to our business and, by necessity and circumstance, include some amounts which were determined using management's best judgments and estimates with appropriate consideration to materiality. Management is responsible for the integrity and objectivity of the financial statements and other financial data included in this report. To meet this responsibility, management maintains a system of internal accounting controls to provide reasonable assurance that assets are safeguarded and that accounting records are reliable. Management supports a program of internal audits and internal accounting control reviews to provide reasonable assurance that the system is operating effectively.

The Board of Directors pursues its responsibility for reported financial information through its Audit Review Committee. The Audit Review Committee meets periodically and, when appropriate, separately with management, internal auditors and the independent auditors, Deloitte & Touche LLP, to review each of their respective activities.



James Wood
*Chairman of the Board
and Co-Chief Executive Officer*



Christian W.E. Haub
*President and
Co-Chief Executive Officer*



Fred Corrado
*Vice Chairman of the Board
and Chief Financial Officer*

Independent Auditors' Report

To the Shareholders and Board of Directors of The Great Atlantic & Pacific Tea Company, Inc.:

We have audited the accompanying consolidated balance sheets of The Great Atlantic & Pacific Tea Company, Inc. and its subsidiary companies as of February 22, 1997 and February 24, 1996 and the related consolidated statements of operations, shareholders' equity and cash flows for each of the three fiscal years in the period ended February 22, 1997. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, such consolidated financial statements present fairly, in all material respects, the financial position of The Great Atlantic & Pacific Tea Company, Inc. and its subsidiary companies at February 22, 1997 and February 24, 1996 and the results of their operations and their cash flows for each of the three fiscal years in the period ended February 22, 1997 in conformity with generally accepted accounting principles.

As discussed in Notes to Consolidated Financial Statements, in fiscal 1994 the Company changed its method of accounting for postemployment benefits to conform with Statement of Financial Accounting Standards No. 112.

Deloitte + Touche LLP

Parsippany, New Jersey
April 24, 1997

Five-Year Summary of Selected Financial Data

The Great Atlantic & Pacific Tea Company, Inc.

	Fiscal 1996 (52 weeks)	Fiscal 1995 (52 weeks)	Fiscal 1994 (52 weeks)	Fiscal 1993 (52 weeks)	Fiscal 1992 (52 weeks)
<i>(Dollars in thousands, except per share data)</i>					
Operating Results					
Sales	\$10,089,014	\$10,101,356	\$10,331,950	\$10,384,077	\$10,499,465
Income (loss) from operations	169,303	151,734	(57,530)	68,280	44,306
Depreciation and amortization	230,748	225,449	235,444	235,910	228,976
Interest expense	73,208	73,143	72,972	63,318	66,436
Income (loss) before cumulative effect of accounting changes	73,032	57,224	(166,586)	3,959	(98,501)
Cumulative effect on prior years of changes in accounting principles:					
Postemployment benefits	—	—	(4,950)	—	—
Income taxes	—	—	—	—	(64,500)
Postretirement benefits	—	—	—	—	(26,500)
Net income (loss)	73,032	57,224	(171,536)	3,959	(189,501)
Per Share Data					
Income (loss) before cumulative effect of accounting changes	1.91	1.50	(4.36)	.10	(2.58)
Cumulative effect on prior years of changes in accounting principles:					
Postemployment benefits	—	—	(.13)	—	—
Income taxes	—	—	—	—	(1.69)
Postretirement benefits	—	—	—	—	(.69)
Net income (loss)	1.91	1.50	(4.49)	.10	(4.96)
Cash dividends	.20	.20	.65	.80	.80
Book value per share	23.27	21.53	20.27	26.02	27.06
Financial Position					
Current assets	1,231,379	1,174,935	1,193,731	1,230,339	1,221,492
Current liabilities	1,016,005	983,968	1,096,454	1,151,132	1,164,723
Working capital	215,374	190,967	97,277	79,207	56,769
Current ratio	1.21	1.19	1.09	1.07	1.05
Expenditures for property	296,878	236,139	214,886	267,329	204,870
Total assets	3,002,672	2,860,847	2,894,788	3,098,695	3,090,930
Current portion of long-term debt	18,290	13,040	112,821	77,755	104,660
Current portion of capital lease obligations	12,708	13,125	14,492	16,097	18,021
Long-term debt	701,609	650,169	612,473	544,399	414,301
Long-term portion of capital lease obligations	137,886	129,887	146,400	162,866	182,066
Total debt	870,493	806,221	886,186	801,117	719,048
Debt to total capitalization	.49	.49	.53	.45	.41
Equity					
Shareholders' equity	890,072	822,785	774,914	994,417	1,034,330
Weighted average shares outstanding	38,221,329	38,220,333	38,220,333	38,220,351	38,219,395
Number of registered shareholders	8,808	10,010	10,867	11,831	12,309
Other					
Number of employees	84,000	89,000	92,000	94,000	90,000
New store openings	30	30	22	16	11
Number of stores at year end	973	1,014	1,108	1,173	1,193
Total store area (square feet)	30,587,324	31,101,589	33,310,121	34,696,265	34,761,170
Number of franchised stores at year end	49	7	—	—	—
Total franchised store area (square feet)	1,345,786	177,936	—	—	—

Corporate Officers

James Wood
*Chairman of the Board
and Co-Chief Executive Officer*

Christian W.E. Haub
*President and
Co-Chief Executive Officer*

Fred Corrado
*Vice Chairman of the Board and
Chief Financial Officer*

Gerald L. Good
*Executive Vice President,
Marketing and Merchandising*

George Graham
*Executive Vice President,
U.S. Operations*

Aaron Malinsky
*Executive Vice President,
Development and Strategic
Planning*

Peter J. O'Gorman
*Executive Vice President,
International Store and Product
Development*

Ivan K. Szathmary
*Executive Vice President,
Chief Services Officer*

Clifford J. Horler
*Senior Vice President,
Design and Construction*

H. Nelson Lewis
*Senior Vice President,
Human Resources*

Brian Pall
*Senior Vice President,
Development*

Michael J. Rourke
*Senior Vice President,
Communications and
Corporate Affairs*

Michael Stolarz
*Senior Vice President,
Sales*

Robert G. Ulrich
*Senior Vice President,
General Counsel*

Peter R. Brooker
*Vice President, Planning
and Corporate Secretary*

Stephen T. Brown
*Vice President,
Labor Relations*

Timothy J. Courtney
Vice President, Taxation

Donald B. Dobson
*Vice President,
Southern Operations*

R. Paul Gallant
President, Compass Foods

R. Terrence Galvin
Vice President, Treasurer

Kenneth W. Green
*Vice President,
Produce Merchandising
and Procurement*

Joseph J. Hoffman
*Vice President,
Meat Merchandising
and Procurement*

Robert A. Keenan
*Vice President,
Chief Internal Auditor*

Francis X. Leonard
*Vice President,
Real Estate Administration*

Mary Ellen Offer
*Vice President,
Assistant Corporate Secretary
and Senior Counsel*

Richard J. Scola
*Vice President,
Real Estate Law and
Assistant General Counsel*

Kenneth A. Uhl
Vice President, Controller

William T. Wolverton
*Vice President, Warehousing
and Transportation*

Canadian Company

J. Wayne Harris
*Chairman and
Chief Executive Officer -
Canadian Company*

Greater Metro New York

William Louttit
*Chairman and
Chief Executive Officer -
Greater Metro New York
Area Operations*

Midwest

Craig C. Sturken
*Chairman and
Chief Executive Officer -
Midwest Operations*

Directors

James Wood (c)(d)(e)
*Chairman of the Board
and Co-Chief Executive Officer*

John D. Barline, Esq. (e)
*Williams, Kastner & Gibbs LLP,
Tacoma, Washington*

Rosemarie Baumeister (b)
*Executive Vice President,
Tengelmann
Warenhandelsgesellschaft,
Germany*

Fred Corrado (c)(d)(e)
*Vice Chairman of the Board and
Chief Financial Officer*

Christopher F. Edley (a)(b)(c)(e)
*President Emeritus and former
President and Chief Executive
Officer of the United Negro
College Fund, Inc.*

Christian W.E. Haub (c)(d)(e)
*President and
Co-Chief Executive Officer*

Helga Haub (c)(d)

Barbara Barnes Hauptfuhrer
(a)(c)(d)(e)
Director of various corporations

William A. Liffers (a)(c)
*Former Vice Chairman of
American Cyanamid Company*

Fritz Teelen (d)
*Chief Operating Officer of
Tengelmann
Warenhandelsgesellschaft,
Germany*

R.L. "Sam" Wetzel (a)(b)(d)(e)
*President and Chief
Executive Officer of Wetzel
International, Inc.*

(a) Member of
*Audit Review Committee,
William A. Liffers, Chairman*

(b) Member of
*Compensation Policy Committee,
Christopher F. Edley, Chairman*

(c) Member of Executive Committee,
James Wood, Chairman

(d) Member of Finance Committee,
R.L. "Sam" Wetzel, Chairman

(e) Member of Retirement
*Benefits Committee,
Barbara Barnes Hauptfuhrer,
Chairman*

Shareholder Information

Executive Offices

Box 418
2 Paragon Drive
Montvale, NJ 07645
Telephone 201-573-9700

Transfer Agent and Registrar

American Stock Transfer and Trust Company
40 Wall Street
New York, NY 10005
Telephone 212-936-5100

Independent Auditors

Deloitte & Touche LLP
Two Hilton Court
Parsippany, NJ 07054

Shareholder Inquiries and Publications

Shareholders, security analysts, members of the media and others interested in further information about the Company are invited to contact the Corporate Affairs Department at the Executive Offices in Montvale, New Jersey.

Internet users can access information on A&P at: www.aptea.com

Correspondence concerning shareholder address changes should be directed to:

American Stock Transfer and Trust Company
40 Wall Street
New York, NY 10005
Telephone 212-936-5100

Form 10-K

Copies of Form 10-K filed with the Securities and Exchange Commission will be provided to shareholders upon written request to the Secretary at the Executive Offices in Montvale, New Jersey.

Annual Meeting

The Annual meeting of Shareholders will be held at 10:00 a.m. on Tuesday, July 15, 1997 at the Sheraton Crossroads Hotel, One International Boulevard, Mahwah, New Jersey. Shareholders are cordially invited to attend.

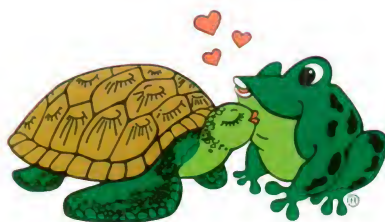
Common Stock

Common stock of the Company is listed and traded on the New York Stock Exchange under the ticker symbol "GAP" and has unlisted trading privileges on the Boston, Midwest, Philadelphia, Cincinnati, and Pacific Stock Exchanges. The stock is reported in newspapers and periodical tables as "GtAtPe."



The Great Atlantic & Pacific Tea Company, Inc.

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recycled paper.*